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No. 86-489

In the Supreme Court of the United States

OCTOBER TERM, 1986

W.T. LANGLEY AND MARY ANN GRIMES LANGLEY,
PETITIONERS

v.

FEDERAL DEPOSIT INSURANCE CORPORATION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

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QUESTION PRESENTED

Whether the court of appeals correctly held that when the Federal Deposit Insurance Corporation (FDIC) acquires assets of an insolvent bank pursuant to a purchase and assumption transaction, the FDIC is shielded by 12 U.S.C. 1823(e) from a claim that an oral side agreement invalidates written loan documents.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. A1-A18) is reported at 792 F.2d 541. The opinion of the district court (Pet. App. A19-A25) is reported at 615 F. Supp. 749.

JURISDICTION

The judgment of the court of appeals was entered on June 25, 1986. The petition for a writ of certiorari was filed on September 23, 1986. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATUTE INVOLVED

12 U.S.C. 1823(e) provides:

> No agreement which tends to diminish or defeat the right, title or interest of the [Federal Deposit Insurance] Corporation in any asset acquired by it under this section, either as security for a loan or by purchase, shall be valid against the Corporation unless such agreement (1) shall be in writing, (2) shall have been executed by the bank and the person or persons claiming an adverse interest thereunder, including the obligor, contemporaneously with the acquisition of the asset by the bank, (3) shall have been approved by the board of directors of the bank or its loan committee, which approval shall be reflected in the minutes of said board or committee, and (4) shall have been, continuously, from the time of its execution, an official record of the bank.

STATEMENT

1. This case arises from the appointment of the Federal Deposit Insurance Corporation (FDIC) as receiver for the Planters Trust & Savings Bank of Oppelousas, Louisiana (Planters) on May 18, 1984. Following Planters' failure, the FDIC arranged a purchase and assumption of Planters' assets. As part of that transaction, the FDIC, acting in its corporate capacity, acquired a portion of those assets, including a $450,000 note executed by petitioners (Pet. App. A4, A10-A11). The note constituted one step in a larger transaction in which petitioners purchased a farm. Petitioners allege that Planters' officials orally made the following representations which were material to that transaction (Pet. App. A4, A5, A7, A9):

(1) that the purchase price would be 100% financed;

(2) that petitioners would have no personal liability on their loans or guaranties;

(3) that no payments would be due until the property was resold;

(4) that petitioners would be provided a purchaser following the closing;

(5) that petitioners would realize a large profit upon reselling the property;

(6) that the property consisted of 1,628.4 acres;

(7) that the property included 400 mineral acres; and

(8) that there were no mineral leases on the property.

None of these alleged representations was disclosed in any of the transaction documents. Rather, the note contained an unconditional promise by petitioners to be fully obligated and liable for payment of the debt (as did the mortgage and personal guaranties also executed by petitioners as part of the transaction). Pet. App. A3.

2. Petitioners eventually defaulted on their obligations to Planters recited in the note. On September 26, 1983, Planters sued for nonpayment (Pet. App. A3). Petitioners responded by bringing a separate action against Planters and its officers alleging that petitioners had been fraudulently induced to sign the note (Pet. App. 5).[1] Following Planters' failure and the FDIC's acquisition of assets including the

[1] The actions were consolidated in the federal district court where Planters' collection suit was still pending (Pet. App. 4).

note, the FDIC, acting in its corporate capacity, was substituted as plaintiff in the pending collection suit and moved for summary judgment (Pet. App. 4-6). The district court granted the motion, ruling that 12 U.S.C. 1823(e) precluded petitioners from avoiding liability on the ground that the loan documents did not fully set forth their understanding with Planters (Pet. App. A6).

3. On appeal, petitioners conceded that Section 1823(e) precluded them from relying on many of the alleged misrepresentations to defeat FDIC's entitlement to payment (Pet. App. A6). Specifically, petitioners acknowledged that they could not rely on misrepresentations that were "promissory," a term which they defined to include the alleged representations concerning the nonrecourse nature of the loan, the absence of any payment obligation until resale, and the promise to find a subsequent purchaser (Pet. App. A7). Petitioners argued, however, that other representations (*e.g.*, the total acreage of the property and its mineral rights) misstated existing facts, and were therefore not governed by Section 1823(e). Pet. App. A7. The court of appeals rejected petitioners' attempt to distinguish, for Section 1823(e) purposes, between promissory and factual misrepresentations. The court explained that Section 1823(e) is intended to ensure that all material terms of an obligor's agreement with a bank are disclosed in the records of the bank (Pet. App. A9-A10). To allow a distinction between promissory fraud and factual fraud would defeat this purpose and would create, the court stated, an "unacceptable 'end run' around § 1823(e)" (Pet. App. A17).

ARGUMENT

The court of appeals carefully considered and correctly decided the issue presented here. Its decision does not conflict with any decision of this Court or of any other court of appeals. Accordingly, the case does not warrant further review.

1. Petitioners contend (Pet. 12-23) that factual misrepresentations should be distinguished from promissory misrepresentations for Section 1823(e) purposes. Under petitioners' view of the statute, the FDIC is protected from defenses based upon false promises made by bank officials but not from defenses based upon false statements of fact by officials of the failed bank. The court of appeals correctly ruled that the distinction urged by petitioners—between the oral *promises* and the oral *warranties* they say were contained in an undisclosed side agreement—is not supported by the statute and is not meaningful in this context (Pet. App. A16-A17).

Congress created the FDIC in order to stabilize and protect the nation's banking system (Pet. App. A8). To that end, the FDIC performs several critical functions, including the examination of banks and the insurance of deposits. *Id.* at A10; 12 U.S.C. 1811 *et seq.* Through its examinations the FDIC is able to decide whether to insure a bank at the outset, whether to terminate insurance, and whether to take measures to correct unsound banking practices. Recognizing the importance of this function, Congress enacted Section 1823(e) to ensure that bank examiners may rely on bank records in critical decisions often made under extreme time pressure.[2] If banks

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[2] When a bank is closed by its chartering authority, the FDIC must quickly determine whether to pay the insured statutory amounts from the Permanent Insurance Fund while

and borrowers were permitted to keep material terms of their transactions unwritten, the FDIC could not adequately assess a bank's strength (Pet. App. A9-A10).

When the FDIC purchases a failed bank's assets, Section 1823(e) protects the FDIC from claims made by debtors that the bank's assets are saddled with unknown liabilities (*FDIC* v. *La Rambla Shopping Center, Inc.*, 791 F.2d 215 (1st Cir. 1986)).[3] Peti-

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the failed bank's receiver liquidates the assets of the estate to pay uninsured depositors and other creditors (12 U.S.C. 1821(f)) or to take the less drastic step of arranging a purchase and assumption transaction (12 U.S.C. 1823(c)(2)(A)). The many advantages of the purchase and assumption alternative are well-recognized, most notably, that the assuming bank generally reopens the failed bank on the next business day, thereby preventing any loss or inconvenience to depositors and any interruption of vital banking services. In order to preserve this advantage, it is imperative that the FDIC consummate the purchase and assumption transaction as quickly as possible. But the statutory authorization for the purchase and assumption alternative is generally limited to situations where the costs to the Permanent Insurance Fund are less than they would be in a straight insurance payoff (12 U.S.C. 1823(c)(4)(A)). Consequently, Section 1823(e) plays a crucial role, for if a bank's records could not be relied upon to ascertain the bank's assets, the FDIC would be unable quickly and fully to discharge its duty of determining what course to follow in disposing of those assets (Pet. App. A10).

[3] As the courts have consistently held, Section 1823(e) shields the FDIC from a host of defenses, including, for example, claims that the debtor never received the consideration for the loan (*FDIC* v. *Fonseca*, 795 F.2d 1102 (1st Cir. 1986)); that the loan was to have been extended and rewritten at a lower interest rate (*FDIC* v. *Vestring*, 620 F. Supp. 1271 (D. Kan. 1985)); that debtors were to receive further financing (*FDIC* v. *Lattimore Land Corp.*, 656 F.2d 139 (5th Cir. 1981)); that debtors would not be personally liable (*FDIC* v.

tioners attempt to distinguish this case from the general rule by segregating the undisclosed side representations they say were made to them into two categories: promissory and factual misrepresentations (Pet. 20-21). They concede (*id.* at 20) that Section 1823(e) shields the FDIC from those claims based on alleged false promises by the bank.[4] But petitioners contend, as they did unsuccessfully in the court of appeals, that their claims regarding false state-

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Hoover-Morris Enterprises, 642 F.2d 785 (5th Cir. 1981)); that the maker's liability would be limited to his trustee capacity (*FDIC* v. *Armstrong*, 784 F.2d 741 (6th Cir. 1986)); that the partners guaranteeing the debt were to be collectively liable only for a portion of the debt (*FDIC* v. *Castle*, 781 F.2d 1101 (5th Cir. 1986)); and that there had been an accord and satisfiaction (*Public Loan Co.* v. *FDIC*, 803 F.2d 82 (3d Cir. 1986)).

In many of these cases the debtors contended, as petitioners do here (Pet. App. 12-14, 20-21), that they were not seeking to enforce an oral agreement which limited the value of their note, but to completely invalidate the fraudulently induced transaction. The courts have routinely held that Section 1823(e) bars such fraud defenses against the FDIC. See, *e.g.*, *FDIC* v. *Armstrong*, *supra*; *FDIC* v. *Castle*, *supra*; *FDIC* v. *Hatmaker*, 756 F.2d 34 (6th Cir. 1985); *FDIC* v. *W.H. Venture*, No. 84-5673 (E.D. Pa. May 22, 1986); *FDIC* v. *Vestring*, *supra*; *FDIC* v. *Rodenberg*, 571 F. Supp. 455 (D. Md. 1983); *FDIC* v. *Rockelman*, 460 F. Supp. 999 (E.D. Wis. 1978).

[4] Indeed, by signing a note that was unconditional and enforceable under its terms, while entering into an alleged oral side agreement that the note would not be enforced, petitioners entered into exactly the kind of "scheme or arrangement" that was condemned by this Court in *D'Oench, Duhme & Co.* v. *FDIC*, 315 U.S. 447 (1942). Having joined such an arrangement, petitioners may not now escape their obligation by claiming that they were in turn defrauded by a co-participant in the scheme. See *British Columbia Investment Co.* v. *FDIC*, 420 F. Supp. 1217 (S.D. Cal. 1976).

ments as to the acreage and mineral rights are beyond the scope of Section 1823(e) and are sufficient in themselves to invalidate the note. The court of appeals correctly perceived that petitioners were in essence alleging that portions of an oral side agreement—"oral warranties" (Pet. App. A17)—had the effect of rendering unenforceable their written promises; and the court correctly concluded that the proffered defense would allow an unacceptable "end run" around the statute (*ibid.*). As the Fifth Circuit explained in an earlier case, "[i]f an obligor may successfully void a note and recoup damages against the FDIC based on a claim of fraudulent inducement from an unwritten agreement, he will have made an end run around § 1823(e) by asserting as fraudulent the same unwritten agreement of which a breach resulting in damages may not under § 1823(e) be asserted against the FDIC." *FDIC* v. *Lattimore Land Corp.*, 656 F.2d 139, 146 n.13 (1981).[5]

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[5] Petitioners also contend (Pet. 12-18) that the decision below creates a circuit conflict on the question whether Section 1823(e) contemplates a distinction between promissory and factual fraud. There is, however, no conflict between this case and *Gunter* v. *Hutcheson*, 674 F.2d 862 (11th Cir.), cert. denied, 459 U.S. 826 (1982). The court below distinguished *Gunter* on its facts, explaining that the approach adopted by the Eleventh Circuit was inappropriate to the particular allegations in this case (Pet. App. A15 n.5). In any event, the court in *Gunter* held on other grounds that the FDIC was immune from claims of fraud in the underlying transaction. Petitioners also cite *FDIC* v. *Hatmaker*, 756 F.2d 34 (6th Cir. 1985), in support of their contention that a conflict exists (Pet. 17-18). In *Hatmaker*, however, the Sixth Circuit held that a debtor was barred from asserting a fraudulent inducement defense against the FDIC under Section 1823(e); its discussion of *Gunter* was dictum.

The promissory/factual fraud distinction urged by petitioners would defeat the purpose of Section 1823 (e), which is to prevent borrowers, and others dealing with a bank, from invoking undisclosed side agreements as defenses against their written obligations after the FDIC has acquired the bank's assets. Such a result would make it impossible for bank examiners to evaluate bank assets or for FDIC officials to assess the viability of purchase and assumption transactions in the manner Congress intended. See note 2, *supra*.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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